

THE ESTABLISHMENT OF A REPRESENTATIVE OFFICE IN RUSSIA

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According to Russian Legislation, foreign legal entities and foreign individuals may carry out business activities in the capacity of different organizational forms. For the pursuit of their business practice in the territory of Russia, foreign legal entities commonly use the following forms:

1. A Representative Office
2. A Russian legal entity:
 - a. Limited Liability Company (OOO);
 - b. Closed Joint-Stock Company (ZAO);
 - c. Open Joint-Stock Company (OAO).

Foreign legal entities are also entitled to establish branch offices in the territory of the Russian Federation.¹

The choice among these forms is primarily based on the intended purpose and scope of activities of the foreign legal entity (the "Company") in the territory of Russia. Should the Company simply require some sort of legal presence in Russia, then its preference is, as a rule, the opening and maintaining of an accredited Representative Office.

This memorandum addresses the general features of a Representative Office in Russia and gives a general overview of the procedures for establishing, utilizing and closing a Representative Office and outlines a comparison with a Branch Office.

¹ See, e.g., Federal Law, "On Foreign Investments in the Russian Federation" of July 09, 1999 No. 160-FZ (as amended), Article 4(3).

I A REPRESENTATIVE OFFICE

According to Russian legislation, a Representative Office in Russia is a separate division of the Company. It is usually established to effectively assist the Company in the execution of cooperation agreements in the areas of trade, economy, finance, science, etc. to develop the exchange of economic, commercial and scientific information and develop trade and economic ties with Russian organizations.

Since a Representative Office is not an independent legal entity, its functions are those inherent in representation activities. Mainly, these are the representation and protection of the Company's interests and support and promotion of the Company's business activities in Russia, etc.

A Representative Office is de jure prohibited from engaging in commercial activities. Thus, the opening of accounts, the obtaining of all necessary licenses and the signing of contracts are usually performed by an authorized officer of the Representative Office based on a respective Power of Attorney issued to him/her by the Company.

II ACCREDITATION OF A REPRESENTATIVE OFFICE

An accredited representation status is obligatory in order for the Company to carry out certain activities in Russia. Further, an accreditation entitles a Representative Office to register cars directly in the name of the Representative Office, obtain visas for Russia for accredited expatriates, employees and the Company's representatives and, which might be of significant importance, duly accredited Representative Offices of companies incorporated in certain countries enjoy VAT exemptions when renting office space.

There are numerous authorized accrediting bodies, many of which accredit Representative Offices on an industry basis. For example, Representative Offices of foreign banks are accredited by the Central Bank of the Russian

Federation; the Chamber of Commerce and Industry ("CCI") issues permits for the opening of Representative Offices of foreign chambers of commerce or other legal entities which cooperate with members of the CCI in Russia etc.

Most Companies are accredited by the CCI of the Russian Federation and the State Registration Chamber of the Russian Federation Ministry of Justice ("SRC").

Accreditation is normally granted for a period of one, two or three years, and this period may be extended thereafter.

Usually, it takes 21 work days to obtain a Permit to open a Representative Office (commencing from the day all the necessary documents are provided to the relevant registration authority). The period of registration may be shortened to 7 work days if necessary. Russian Legislation provides for the following three categories of Companies that may have their Representative Offices accredited:

1. companies which are prominent in the world markets and have positive records as affiliates of Russian organizations in various fields;
2. Companies which are engaged in co-production arrangements with Russian enterprises, agencies and other organizations or which are interested in developing trade and economic ties with Russia; and
3. Companies that are parties to major agreements for scientific and technological cooperation and other activities with Russian organizations.

Russian Legislation expressly states that accreditation may also be granted on the basis of inter-governmental agreements concluded with other countries. In practice, these requirements do not need to be strictly complied with, and it is not very difficult for a Company to obtain

permission to open and maintain a Representative Office in Russia.

From the procedural point of view, it is easier to accredit a Representative Office of a foreign legal entity than to register a new legal entity with the participation of foreign capital. Moreover, there are some benefits to an accredited Representative Office, as mentioned above; fewer administrative, tax reporting and accounting obligations; a Representative Office is considered to be a non-resident for Russian currency control purposes; it may also benefit from a relevant double taxation treaty (if any).

III COMMERCIAL ACTIVITIES OF A REPRESENTATIVE OFFICE

When contemplating the establishment of a Representative Office, the Company must pay special attention to the scope of the activities authorized either by law or by the requirements of the accrediting authority. Russian Legislation stipulates the following two activities as authorized:

1. to effectively assist in the implementation of cooperation agreements in the areas of trade, economy, finance, science and technology, transport, tourism, and others; and to seek opportunities for further developing such co-operation, for example, the exchange of economic, commercial, scientific and technological information and to develop trade and economic ties with Russian organizations; and
2. to facilitate commercial and other transactions with, and render effective assistance to, Russian organizations in connection with the:
 - a. exportation of machinery, equipment, and other goods and services;
 - b. introduction of the newest achievements in global technology;

- c. importation of modern machinery and equipment; and
- d. performance of technical services.

The outline above is general and a Company seeking accreditation may need to discuss the activities that are specifically allowed under the terms of a particular accreditation with the accrediting authorities.

Representative Offices are prohibited from engaging in commercial activities within Russia, and, consequently, they are not subject to Russian corporate income tax (profit tax). In practice, however, it turns out that many Representative Offices conduct commercial activities that should, in effect, be carried out by either a Branch Office or a Russian legal entity. To date, the Russian authorities have generally not taken prohibitory actions against such activities if a Representative Office is registered with the Russian tax authorities and pays tax on its profits.

Still, it is difficult to predict the policy that the Russian authorities will pursue in the future towards commercial Representative Offices.

A Representative Office is subject to fewer tax reporting and accounting obligations than a Branch or a Russian legal entity. The profits of the Company on its business activities in Russia are not subject to taxation provided that the activities of a Representative Office do not meet the criteria of a Permanent Establishment². Therefore, a Representative Office and its employees shall not engage in activities other than the:

1. use of facilities for the purposes of storage, demonstration, or supply of goods or manufactured objects owned by an expatriate employee or the Company;
3. storage of goods and manufactured objects owned by the Company for the purposes of demonstration or supply;
4. storage of goods and manufactured objects owned by the Company for the purpose of their processing by another individual or legal entity;
5. maintenance of a permanent place of activities for the purpose of purchasing goods or manufactured objects or for the collection of information on behalf of the Company;
6. maintenance of a permanent place of activity for the purpose of carrying out other activities of a preparatory or subsidiary nature on behalf of the Company; and
7. maintenance of a permanent place of activity for the purpose of carrying out any combination of the activities specified above.

If a Company is considered to have a Permanent Establishment in Russia (e.g., if a Representative Office carries out commercial activities), the Company will, in principle, be obligated to pay tax on profits originating from the commercial activities in Russia and the Russian authorities may demand the submission of information in the form of accounting or otherwise. If such demand is not complied with, the authorities may make an arbitrary estimate of the Company's profits from its operations in Russia and, accordingly, apply tax on "assumed profits". In practice, some Representative Offices engage in activities other than those stipulated by the Regulations; for example, the provision of services directly to clients in Russia. However, such activities may be grounds for the closure of a Representative Office and could result in a liability for

² As defined in the Tax Code of the RF, Part 2, August 5, 2000 (as amended), Article 307 and in the State Tax Service Instruction N34 On the Taxation of Profits and Income of Foreign Entities, June 16, 1995, Permanent Establishment, for taxation purposes, means a branch, representative office (named in the Tax Code), division, bureau, office, agency, any other separate division or any other place of activity of such entity whereby an entity carries out business activity in Russia (as formulated in the above-mentioned legislation) with the purpose to profit from such activity.

corporate income tax (profit tax) under applicable Russian tax rules. Information on specific cases is exchanged between foreign and Russian tax authorities at their request.

When planning the work of an expatriate or a local employee, due consideration should be given to the concept of "Qualified Agent". If the intended purpose is carefully and correctly formulated, an employee may stay and work in Russia for the Company without being characterized as a "Qualified Agent". In that respect, it is important that the employee has a power of attorney that is very specific and does not authorize the employee to formally and generally sign contracts for and on behalf of the Company.

IV AUTHORITIES AND PROCEDURES FOR ACCREDITATION AND REGISTRATION

The opening of a Representative Office in Russia requires accreditation with the State Registration Chamber, the Chamber of Commerce and Industry, or some other accrediting authority and registration with the following government bodies and agencies:

- State Registration Chamber (if a Representative Office is accredited with the Chamber of Commerce and Industry or any other accrediting authority other than the State Registration Chamber);
- Federal Tax Service;
- Statistics Service;
- Pension Fund;
- Fund of Social Insurance;
- Fund of Obligatory Medical Insurance.

V DOCUMENTS REQUIRED FOR THE OPENING (ACCREDITATION) OF A REPRESENTATIVE OFFICE

1. Extract from the Company Register certifying the registration of the Company in the country of origin.
2. Certificate from the tax authorities stating that the Company is a taxpayer in its country of origin. The certificate must include the Company's taxpayer identification number.
3. Letter of good standing from the Company's bank attesting to the solvency of the Company.
4. A copy of the charter of the Company.
5. Original resolution passed by the Board of Directors or other authorized body of the Company to open a Representative Office in Russia; to approve of the regulations of a Representative Office; and to appoint the head of the Representative Office.
6. Original application for permission to establish a Representative Office (written on the Company's letterhead) addressed to the head of the accreditation authority and signed by the General Manager of the Company.
7. Original regulations of the Representative Office signed by the General Manager of the Company (or by the head of a Representative Office).
8. Original Power of Attorney signed by the General Manager of the Company authorizing the head of the Representative Office to act in this capacity.
9. At least two original recommendation letters from two different reliable Russian business partners of the Company.

10. Guarantee letter from the landlord of the future office premises or a draft lease Agreement for the Representative Office and a notarized copy of the landlord's Ownership Certificate.
11. Notarized copy of the certificate of registration of the head of the Representative Office as a taxpayer in Russia (if the head of the Representative Office is a Russian citizen).

These documents are the minimum required in order to open (accredit) a Representative Office.

However, the Russian authorities maintain the right to ask for further documentation³.

When and if applicable, all the documents executed in a language other than Russian must be translated into Russian and properly notarized and/or legalized. The obligation to legalize or apostille may be retracted by an international agreement to which the Russian Federation is a party.

VI EXTENSION OF THE ACCREDITATION

If a Company decides to extend the period of accreditation of its Representative Office, it must apply for such renewal before the end of the accreditation period. To prolong the accreditation the following documents are required:

1. Original application for permission to extend the accreditation of the Representative Office, written on the Company's letterhead and signed by the General Manager of the Company or by the Head of the Representative Office, sealed with a Company stamp. The

application also must include the number of the original Permission to open the Representative Office, the date of its issue, the period of validity and the purpose of the extension.

2. Original Business report of the Representative Office for the entire period of previous accreditation, written on the Company's letterhead and signed by the Head of the Representative Office and including the following information: activity report, business cooperation with Russian partners, purpose of extending the accreditation and number of accredited employees and cars imported.
3. Letter of good standing from the Company's bank attesting to the solvency of the Company.
4. Notarized copy of the document, confirming the Representative Office's registration with the Russian tax authorities; including the Company's identification tax number.
5. Letters from Russian Banks confirming the opening of the Company accounts.
6. Original Permission to open a Representative Office.
7. Original Certificate of entering the Representative Office into the State Register.
8. Notarized copy of the Power of Attorney granting the Head of the Representative Office respective powers.
9. Notarized copy of the Power of Attorney authorizing an individual to perform all the necessary actions in view of the extension of the accreditation of the Representative Office with the State Registration Chamber.

The Russian authorities have the right to ask for further documentation. When and if applicable,

³ Regulations On the Procedure of Establishing Representative Offices of Foreign Companies, Banks and Organizations and their activities in the USSR, November 30, 1989, Article 5

all the documents executed in a language other than Russian must be translated into Russian and properly notarized and/or legalized.

VII CLOSING A REPRESENTATIVE OFFICE

A Representative Office of a Company may be closed down in the following circumstances:

- per the expiration of the term of accreditation of the Representative Office;
- if the Company is liquidated;
- when the inter-governmental agreements that provided the basis for the establishment of the Representative Office are terminated;
- if the accrediting authority finds that a Representative Office has violated either the conditions under which it was established or Russian law (we are not aware of any Representative Office which has been closed down for these reasons); and
- if the Company decides to close down its Representative Office in Russia.

Whenever one of these events occurs, the terminating party (i.e., the accrediting authority or the Company) must notify the other party of its decision. Thereafter, a Representative Office must dismiss its personnel, vacate all offices and residential premises and cease operations within three months from the date of such notification. The Federal Tax Service must also be informed when a Representative Office ceases to operate.

VIII REPRESENTATIVE OFFICE VS. BRANCH OFFICE.

A foreign legal entity may also conduct its business activities in Russia through a Branch Office. Currently, the legal status and the procedure of accreditation and registration of a Representative Office and a Branch Office differ minimally.

However, under Russian legislation, a Branch Office is a separate division of a company, which carries out all or part of the Company's functions, including the functions of a Representative Office. Neither a Branch Office or a Representative Office is a legal entity.

Both a Representative Office and a Branch Office operate based on the property granted by the Company. Both are acting by virtue of the Regulations approved by the authorized executive body of the company. Managers of a Representative Office and a Branch Office are both appointed by the Company and they both act by virtue of a corresponding Power of Attorney.

However, as opposed to a Representative Office, the Regulations of a Branch Office must include the total cost estimation of the capital which is to be paid into the main funds of the Branch by the foreign legal entity. A Representative Office may be accredited for a period of up to 3 years and a Branch Office up to 5 years. Moreover, there are some types of licenses which can be obtained only by a Branch Office.

Certain aspects of the accreditation procedure may be changed and individual circumstances should be considered when deciding which organizational form would be more effective for certain purposes.

The legal environment regulating the matters dealt with in this bulletin is constantly changing. In the likelihood of your interest, please, do not hesitate to contact us for assistance in your business endeavors in Russia.

Best regards,

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